Emerging Companies Fund

Monthly Update: February 2019

SAVILLE CAPITAL

Dear Fellow Investors,

Our Emerging Companies Fund was up +4.8% in February vs +4.8% for the Emerging Companies Accumulation Index (XECAI) and +7.1% for the Small Industrials Accumulation Index (XSIAI). Since inception the Fund is +67.4% (assuming distributions are reinvested) vs -1.5% for the XECAI, +23.0% for the XSIAI and +9.3% for our cash-based benchmark.

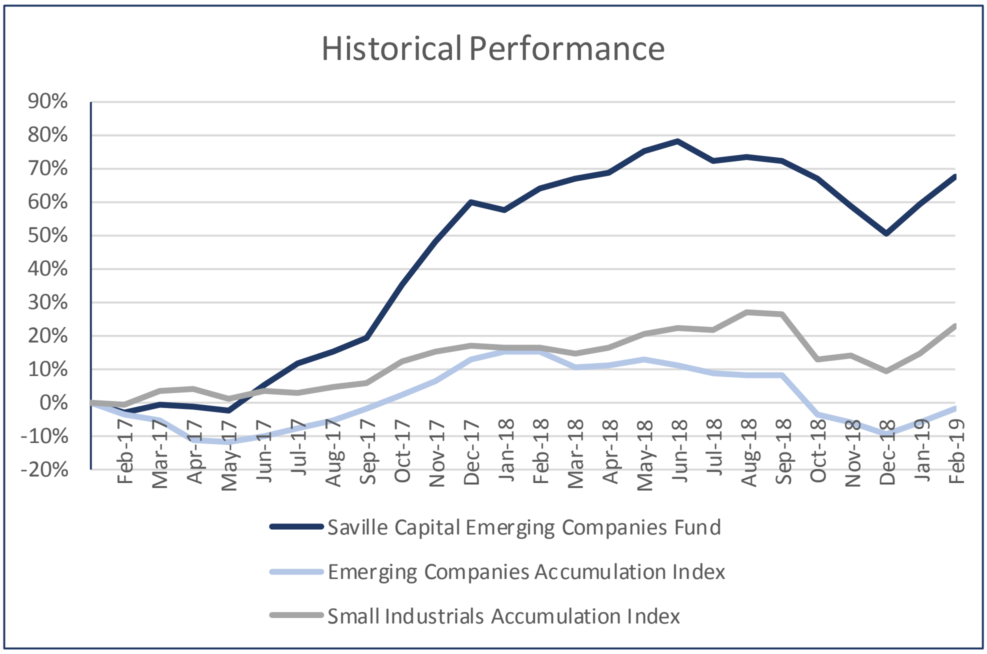
We were pleased to come through another reporting season with very positive results for the portfolio. While market sentiment was clearly supportive, that element is beyond our control. Conversely, ensuring that we are exposed to companies we believe will consistently deliver earnings above market expectations (or at a minimum avoid those that are likely to disappoint) is an essential part of delivering solid performance for the Fund. From our perspective, and as generally endorsed by subsequent share price performance, none of the companies we own reported unexpectedly poor results this month. Furthermore, several delivered earnings that were ahead of expectations, whether that be explicit consensus or what could reasonably be derived from the share price.

What is also important to note, but isn't obvious from the headline numbers, is that much of our positive performance came from what we consider lower risk investments – most notably, Think Childcare (TNK, +27%) and National Veterinary Care (NVL, +13%). As such, we think our Fund's results were built on solid foundations, as opposed to being based on an accelerating shift in positive sentiment towards highly speculative stocks in either resources or technology (a theme which was clearly prevalent during February).

Performance summary

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total	3M	12M
2017		-3.2%	+2.6%	-0.6%	-1.0%	+7.6%	+6.4%	+2.7%	+4.0%	+13.2%	+9.5%	+8.1%	+60.1%		
2018	-1.6%	+4.2%	+1.6%	+1.1%	+4.1%	+1.6%	-3.1%	+0.7%	-0.8%	-3.2%	-4.8%	-5.2%	-5.9%		
2019	+6.0%	+4.8%											+11.1%	+5.3%	+1.9%

Returns are net of all base fees, performance fees and expenses of the Fund



Performance commentary

Apart from TNK and NVL, the other key positive contributors to the Fund's performance in February were Polynovo (PNV, +16%), Audinate (AD8, +28%), Bluechiip (BCT, +7%), and Redbubble (RBL, +4%). The key negative contributor was Rhinomed (RNO, -24%) which declined on very light volumes, but perhaps also in a delayed reaction to the somewhat disappointing headline revenue figures in its 2Q result released in late January.

There was limited new material information in PNV's 1H FY19 accounts given it had already reported its 1H revenue. However, we were pleased to see that operating expenses came in below our expectations, demonstrating good cost discipline, which is unusual for an early stage growth company. Furthermore, the sales breakdown by geography showed that initial sales in Australia and New Zealand were well ahead of our expectations and imply significant market share gains from the incumbent provider, which bodes well for PNV's likely penetration of other sophisticated healthcare markets around the world.

The only new information we received in PET's latest report was CY19 revenue guidance of $27m - $30m (+55% on pcp) and Net Profit Before Tax of $6m - $8m (+100% on pcp). While this was slightly below our own forecast and what one might have extrapolated from previous guidance for FY19, it is still exceptional growth. More importantly, based on its growing pipeline of projects across China, the Americas and Europe, we think these current growth rates can be sustained into the foreseeable future, which underpins our positive view on the stock and should see its share price re-rate higher over time.

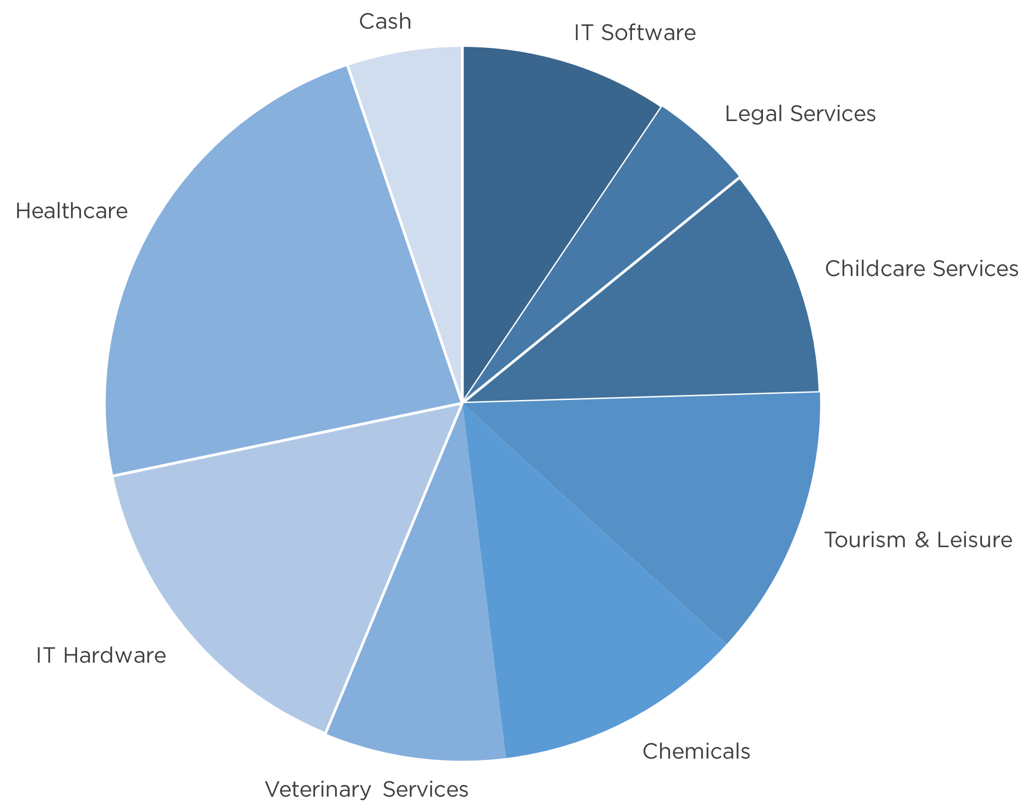
After a tumultuous six months for its share price, TNK reported a CY18 result that was in line with its earnings guidance while also reinstating its dividend, reflecting growing confidence in its earnings outlook. Importantly, TNK was able to highlight that its performance continued to improve into January, with revenue up +9.2% on pcp and its Service performance margin (a proxy for centre-level EBITDA) at 21.2% vs 15.4% in the pcp, driven by a combination of higher occupancy and improved labour utilisation. We still think the outlook for TNK over the next few years is very favourable with solid demand growth (increased Government subsidy), constrained supply growth (tighter lending conditions), significant acquisition growth (pipeline of 73 incubator centres) and reduced opex and capex investment from CY20 onwards (completion of transition to Nido brand).

The only material news for BCT was a published interview with its CEO, Andrew McLellan, in which he referred to having four new OEM proposals under active consideration, some of which came out of two recent trade shows. As a reminder, BCT already has three OEM partnerships, the most significant of which is with Labcon, underpinned by a three-year US$11.3m supply contract. It was also noted that 3Q FY19 volumes and revenues will be up on 2Q FY19, which, while not surprising, at least gives the market confidence that the Labcon contract is now starting to ramp up and volumes will only increase from here.

Finally, after being a very poor performer for the Fund, we exited the remainder of our shareholding in Longtable (LON). It is important to highlight that our decision to sell was not based on its share price performance (if it was, we would have sold out long ago). Like any position in the Fund, we were happy to show patience and not be influenced by weak share price performance or short-term earnings indicators, particularly given the strategic changes being undertaken at its largest asset, Paris Creek. However, what changed our view was that following a 12-month process of rebranding, repricing and repackaging the Paris Creek product portfolio, the market feedback (based on online reviews) has been almost universally negative. This not only has implications for earnings at Paris Creek (which continue to decline), but also our confidence in the strategic direction of the entire LON portfolio. Highlighting that it is never too late to take affirmative action, we believe our decision has already been vindicated following the release of a very poor 1H FY19 result, combined with a deeply discounted (40% below last closing price) capital raising to fund working capital (LON is still burning significant cash at the operating level) and the buyout of the remaining 52% of Maggie Beer Products.

Portfolio characteristics

We currently have 95% of our capital invested in 12 stocks, with two removals since January.



Thanks again for your interest and support and we look forward to providing another update in early April on our performance during March.

Kind regards,

Jonathan Collett

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